



## Disclaimer regarding the Effective date of Handbook 4000.1

- On April 30, 2015, FHA announced that it extended the effective date for the policies contained in the *Single Family Housing Policy Handbook* (SF Handbook; HUD Handbook 4000.1) from June 15, 2015 to September 14, 2015.
- This training session was recorded prior to April 30, 2015. Please note the change of the effective date of SF Handbook during the presentation.



# Modules 4 & 5: Using the TOTAL Mortgage Scorecard and Manual Underwriting

*Single Family Housing Policy Handbook 4000.1  
Title II Insured Housing Program Forward Mortgages  
Origination through Post-Closing/Endorsement*

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## **FHA Single Family Housing Policy Handbook**

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# Objective

- To review some of FHA Single Family policies to effectively conduct both a TOTAL Scorecard and Manual Underwrite evaluation.



# Retirement of the TOTAL Scorecard User Guide

- The **TOTAL Scorecard User Guide** will be retired upon effective date of *HUD Handbook 4000.1 (June 15, 2015)*.
- Unless otherwise specifically announced, the use and the applicable policies of FHA 's Mortgage Scorecard will be contained in, **Section 4, Underwriting the Borrower Using the TOTAL Mortgage Scorecard** in *HUD Handbook 4000.1*.



## How Does TOTAL Work?

- TOTAL is based on a mathematical scorecard equation using several credit variables combined with automated underwriting systems (AUS) functionalities.
- The scorecard element provides **a risk recommendation**.
- The AUS provides the documentation element.



# Automated System Integrity

- The Mortgagee is responsible for the integrity of the data elements entered into the AUS to ensure the valid outcome of the mortgage credit risk evaluation performed by TOTAL.
- The Mortgagee is responsible for having a full understanding on the operating system applications, processes, and procedures it uses to ascertain TOTAL Scorecard risk evaluations.
- TOTAL is a tool and not a substitute for the Mortgagee's reasonable consideration of risk and credit worthiness.



# Automated System Functionality

TOTAL Mortgage Scorecard is available for Mortgagees to use for the purposes of prequalifying mortgage loan applicants.





## Automated System Functionality (cont.)

- FHA will not recognize the risk assessment, nor will information be transmitted from TOTAL Mortgage Scorecard to FHA Connection (FHAC), for endorsement processing without an FHA case number.
- The Mortgagee must score the mortgage at least once after FHA case number assignment.
- It is imperative that Mortgagees enter the FHA case number into their Loan Origination System or AUS as soon as it is assigned and request a scoring event from TOTAL.



## Use of TOTAL Scorecard

- Mortgagees using TOTAL remain solely responsible for prudent underwriting practices and the final underwriting decision.
- Mortgagees are expected to exercise both sound judgment and due diligence in the underwriting of a loan to be insured by FHA.



# Program Scoring Requirements

All transactions must be scored through the TOTAL Mortgage Scorecard, except:

- Streamline Refinance transactions;
- Assumptions; and
- Home Equity Conversion Mortgages (HECMs).



## Feedback Certificate/Finding Report

- Each AUS using the TOTAL Mortgage Scorecard provides a Feedback Certificate/Finding Report, which documents the results of the credit risk evaluation and identifies the credit report utilized for the scoring event.
- The Feedback Certificate/Finding Report upon which the Mortgagee makes its underwriting decision prior to endorsement must be included in the case binder.



## HUD Employee and TOTAL Scorecard

- If the mortgage involves a HUD employee, the Mortgagee must score the transaction through TOTAL.
- If the file receives an **Accept**, the **Mortgagee** must:
  - Underwrite the transaction in accordance with the guidance in the Underwriting the Borrower Using the TOTAL Mortgage Scorecard section;
  - Submit conditional loan for HUD underwriting approval; and
  - Submit the underwritten case binder to the Processing and Underwriting Division Director at the jurisdictional HOC for final underwriting approval.



# The Mortgagee and TOTAL Mortgage Scorecard

The Mortgagee must:

- Submit data to the TOTAL Mortgage Scorecard through an approved AUS vendor in a data format that is acceptable to the AUS vendor as described in the TOTAL Mortgage Scorecard Developer's Guide.



# The Mortgagee and TOTAL Mortgage Scorecard (cont.)

The Mortgagee must:

- Ensure full compliance with all FHA eligibility requirements and all requirements of *HUD Handbook 4000.1*, Section 4., **Underwriting the Borrower Using the TOTAL Mortgage Scorecard.**



# The Mortgagee and TOTAL Mortgage Scorecard (cont.)

The Mortgagee must:

- Verify the information used to score the mortgage through TOTAL, but does not need to analyze the credit history unless otherwise stated in *HUD Handbook 4000.1*, section entitled, **Underwriting the Borrower Using the TOTAL Mortgage Scorecard**, if an Accept or Approve recommendation is received.





# The Mortgagee and TOTAL Mortgage Scorecard (cont.)

The Mortgagee must:

- Verify the **integrity of all data elements entered into the AUS** to ensure the outcome of the mortgage credit risk evaluation from TOTAL Scorecard.



# The Mortgagee and TOTAL Mortgage Scorecard (cont.)

The Mortgagee:

- **May not accept or deny** an FHA-insured mortgage based **solely on a risk assessment generated by TOTAL Mortgage Scorecard.**



# The Underwriter and TOTAL Mortgage Scorecard

The underwriter must:

- Underwrite all appraisals according to standard FHA requirements.
- Conduct a manual underwrite on mortgage applications where TOTAL issues a **Refer** decision.



# Automated Underwriting System Data Entry Requirements

The Mortgagee:

- Must verify the integrity of the data elements entered into the AUS to ensure the outcome of the mortgage credit risk evaluation performed by TOTAL is valid.
- These data elements include:
  - Borrower's Credit Report;
  - Borrower's Liabilities/Debt;
  - Borrower's Effective Income;
  - Borrower's Assets/Reserves;
  - Adjusted Value; and
  - Borrower's Total Mortgage Payment including Principal, Interest, Taxes, and Insurance (PITI).



# Automated Underwriting System Data Entry Requirements: Third-Party Originators

- The Mortgagee may permit a sponsored Third-Party Originator (TPO) to enter data into the AUS.
- Both the Mortgagee and its TPO must ensure and verify all data entered into the AUS.
- The **Mortgagee remains ultimately responsible** for ensuring the data entered into the AUS is correct.



## New Versions of TOTAL Mortgage Scorecard

- From time to time, FHA will release new versions of the TOTAL Mortgage Scorecard. FHA will announce the date that the new version will be implemented.
- All mortgages being scored for the first time will be scored using the new version. For mortgages with a case number, the mortgages will be scored using the version that was effective when the case number was assigned.
- Existing mortgages scored without a case number will be scored according to the version number tag that is provided in the TOTAL file by the AUS provider (if **none**, then the **current version** will be used).
- All mortgages without a case number will be scored using the new version 90 days after the new version is implemented.



## Risk Classification

- If the Feedback Certificate/Finding Report shows an Accept or Approve, it will be referred to as Accept.



## The Recommendation

### Accept or Refer

- Risk Recommendation
- **TOTAL**

### Eligible or Ineligible

- Program / Product
- **AUS**

Regardless of the AUS used to request the scoring event, the same risk recommendation will result.





## The Recommendation (cont.)

Regardless of the AUS used to request the scoring event, the same risk recommendation will result:

- Data integrity; and
- Operating systems applications.
  - LOS
  - AUS



## Recommendation: Accept/Eligible

- If the Feedback Certificate/Finding Report shows an Accept/Eligible recommendation, the mortgage may be eligible for FHA's insurance endorsement provided the Mortgagee verified that:
  - Data entered into the AUS is accurate;
  - All supporting documentation is consistent with the scoring event data elements; and
  - The entire mortgage application complies with all FHA requirements.



## **Recommendation: Accept/Ineligible**

- If the Feedback Certificate/Finding Report shows an Accept/Ineligible recommendation, the Borrower's credit and capacity would meet the threshold for approval, but the mortgage does not fully comply with FHA's eligibility requirements.
- The Mortgagee must analyze the Feedback Certificate and determine if the reason for the ineligibility is one that can be resolved in a manner that complies with FHA underwriting requirements.



## Recommendation: Accept/Ineligible

- If the Mortgagee can correct the reason for ineligibility, **the Mortgagee may rescore the mortgage in the AUS.**
- When the reason for **ineligibility cannot be corrected in the AUS**, the Mortgagee may underwrite the mortgage using the following requirements for an Accept mortgage, but **must resolve the reason for ineligibility in accordance with FHA requirements** and must provide an explanation of the resolution in the remarks section of form [HUD-92900-LT](#), *FHA Loan Underwriting and Transmittal Summary*.



## **Recommendation: Accept/Ineligible (cont.)**

Typical reasons for an Accept/Ineligible recommendation may include but are not limited to:

- Loan amount that exceeds the FHA Statutory Loan Limits;
- Property type submitted does not correspond to the Section of the Act selected in the AUS;
- Insufficient reserves on a 3-or 4 unit property; and
- Insufficient funds for closing.



## Recommendation: Refer

The underwriter must **manually underwrite** any mortgage application for which:

- The Feedback Certificate shows a **Refer** recommendation;
- Any result other than those described in *HUD Handbook 4000.1*, Section 4 Underwriting the Borrower Using the TOTAL Mortgage Scorecard; **or**
- An **Accept** risk classification was manually downgraded.



# Accept Risk Classifications Requiring a Downgrade to Manual Underwriting



# Accept Risk Classifications Requiring a Downgrade to Manual Underwriting

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The mortgage file contains information or documentation that **cannot be entered into or evaluated by TOTAL Mortgage Scorecard**.





## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- Additional information, **not considered in the AUS** recommendation, **effects the overall insurability** of the mortgage.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The Borrower has **\$1,000 or more collectively in Disputed Derogatory Credit** accounts.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The date of the Borrower's bankruptcy discharge as reflected on **bankruptcy documents** is within two years from the **date of case number assignment**.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The **case number assignment date** is within three years of the date of the transfer of title through a foreclosure sale.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The **case number assignment date** is within three years of the date of the transfer of title through a Deed-in-Lieu (DIL) of foreclosure.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage that **received an Accept** recommendation if:

- The Mortgage Payment history requires a downgrade as defined in **Housing Obligations/Mortgage Payment History**.



# Mortgage Payment Downgrade: Obligations/Mortgage Payment History Purchase and No Cash-Out Refinance

## Purchase and No Cash-Out Refinance Transactions

Downgraded to a **Refer** if any mortgage trade line reflects:

Most recent 12 months	$\geq 3 \times 30$ Three or more late payments of greater than 30 Days
	$\geq 1 \times 60 + \geq 1 \times 30$ One or more late payments of 60 Days plus one or more 30-Day late payments.
	$\geq 1 \times 90$ One payment greater than 90 Days late.

\* A Mortgage Payment is considered delinquent if not paid within the month due.

\*\* Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



# Mortgage Payment Downgrade: Obligations/Mortgage Payment History Purchase and No Cash-Out Refinance Transactions (cont.)

## Cash-Out Refinance Transactions

Downgraded to a **Refer** if any mortgage trade line reflects:

- Any delinquency within 12 months of the case assignment date; or
- A current delinquency.

\*A Mortgage Payment is considered delinquent if not paid within the month due.

\*\*Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.





## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting

The Mortgagee **must downgrade** and manually underwrite any mortgage application that **received an Accept** recommendation if:

- The Borrower has an **undisclosed mortgage debt**.



## Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (cont.)

The Mortgagee **must downgrade** and manually underwrite any mortgage application that **received an Accept** recommendation if:

- **Business income shows a greater than 20 percent decline over the analysis period.**



# **Borrower Eligibility Requirements and Underwriting the Borrower Using the TOTAL Mortgage Scorecard**

In the Origination/Processing section under, General Mortgage Insurance Eligibility the new HUD Handbook 4000.1 addresses Borrower Eligibility policies concerning:

- Delinquent Federal Debt and Delinquent Federal Non-Tax Debt;
- Credit Alert Verification Reporting System (CAIVRS); and
- Suspended and Debarred Individuals (Excluded Parties).



# Delinquent Federal Non-Tax Debt **vs.** Delinquent Federal Tax Debt

## **Federal Non-Tax Debt**

CAIVRS (or other means)



Debt Collection Improvement Act



Borrower must resolve their federal non-tax debt in accordance with the **Debt Collection Improvement Act.**



Clear CAIVRS Report

## **Federal Tax Debt**

Does not report on CAIVRS

Delinquency must be resolved (paid satisfied or payment arrangement)



# Applicability of Automated Underwriting System Rules

If the mortgage application must be manually downgraded, the Mortgagee must cease its use of the AUS and comply with all requirements for manual underwriting when underwriting a downgraded mortgage.



## Case Study: Downgrade

Credit Report		
Mortgage	12 months	1 x 30 , 1 x 60
Revolving	12months	0 x 30
Car Loan	12 months	0 x 30
Delinquent Federal Student Loan: CAIVRS		\$7500

- Borrower has applied for FHA purchase transaction.
- Borrower has an established credit history.
- Reflected is the borrower's last 12 months.

An Accept risk classification was received.

Should a downgrade to a manual underwrite be issued?



## Case Study: Downgrade (cont.)

Credit Report		
Mortgage	12 months	1 x 30 , 1 x 60 / One or more late payments of 60 plus one or more 30 day
Revolving	12months	0 x 30
Car Loan	12 months	0 x 30
Delinquent Federal Student Loan: CAIVRS		\$7500 / Not a Downgrade but, Borrower Eligibility

- Borrower has applied for FHA purchase transaction.
- Borrower has an established credit history.
- Reflected is the borrower's last 12 months.

An Accept risk classification was received.

Should a downgrade to a manual underwrite be issued? YES



# Rescoring Requirements

The Mortgagee must rescore a mortgage when:

- Any data element of the mortgage change; and/or
- New Borrower information becomes available.





## Tolerance Levels

The Mortgagee is not required to rescore a mortgage if the following data elements change from the last scoring event within the described tolerance levels:

When assessing...	Rescore is not required if:
Cash Reserves	Cash Reserves verified are not less than 10% below the previously scored amount
Income	Income verified is not less than 5% below the previously scored amount
Tax and Insurance Escrow	The cumulative monthly tax and insurance escrow does not result in more than a 2% increase in the Total Mortgage Payment to Effective Income ratio (PTI)



## Case Study: Tolerance Levels

Original Scoring Event	
Principal & Interest	\$1000
Taxes	200
Insurance	40
HOA	25
Debts	500
TOTAL PTI	\$1265 / 30%
TOTAL Fixed Payment	\$ 1765 / 42%

Changes:	
Principal & Interest	\$1000
Taxes	210
Insurance	65
HOA	77
Debts	500
TOTAL PTI	\$1352 / 32%
TOTAL Fixed Payment	\$ 1852 / 44%

Borrower's Effective Monthly Income \$4250

Is this case required to be rescored through TOTAL?



## Case Study: Tolerance Levels (cont.)

Original Scoring Event	
Principal & Interest	\$1000
Taxes	200
Insurance	40
HOA	25
Debts	500
TOTAL PTI	\$1265 / 30%
TOTAL Fixed Payment	\$ 1765 / 42%

Changes:	
Principal & Interest	\$1000
Taxes	210
Insurance	65
HOA	77
Debts	500
TOTAL PTI	\$1352 / 32%
TOTAL Fixed Payment	\$ 1852 / 44%



Borrower's Effective Monthly Income \$4250

Is this case required to be rescored through TOTAL? NO



## Credit Report Requirements

- The Mortgagee must obtain a credit report with information from at least two credit repositories for each Borrower who will be obligated on the Mortgage Note.



# **Non-Borrowing Spouse Community Property State: Consent and Authorization**

The Mortgagee must obtain a non-borrowing spouse's consent and authorization where necessary to;

- verify specific information required to process the mortgage application, including the consent to verify their SSN with the Social Security Administration (SSA).



## **Credit Report: Non-borrowing Spouse**

- The Mortgagee must obtain a credit report for a non-borrowing spouse who resides in a community property state, or if the subject property is located in a community property state.
- The credit report must indicate the non-borrowing spouse's SSN was matched with the SSA, or the Mortgagee must provide separate documentation indicating that the SSN was matched with the SSA.
- The Mortgagee does not submit the non-borrowing spouse credit report as part of the TOTAL Scorecard risk evaluation.



## **Inconsistencies: Credit Report and Mortgage File**

- The Mortgagee must obtain a new credit report and rescore the mortgage through TOTAL if the underwriter identifies inconsistencies between any information in the mortgage file and the original credit report.



# Evaluating Credit History TOTAL





# **Collection Accounts, Charge Off Accounts, Accounts with Late Payments in the Previous 24 Months, and Judgments**

- An explanation of collection accounts, charge off accounts, accounts with late payments, Judgments, or other derogatory information within the last 24 months is not required.



# Disputed Derogatory Credit Accounts

- **Disputed Derogatory Credit Account** refers to disputed charge off accounts, disputed collection accounts, and disputed accounts with late payments in the last 24 months.



# Disputed Derogatory Credit Accounts: Exclusions

The following accounts can be excluded from consideration in the underwriting analysis:

- Medical accounts; and
- Disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use
  - To exclude these balances, the Mortgagee must include a copy of the police report or other documentation from the creditor to support the status of the accounts.



## Disputed Derogatory Credit Accounts: Applicability

- Credit report utilized by TOTAL Mortgage Scorecard indicates that the Borrower has **\$1,000 or more collectively** in Disputed Derogatory Credit Accounts, the mortgage must be downgraded to a **Refer and manually underwritten**.
- Disputed Derogatory Credit Accounts of a non-borrowing spouse in a community property state **are not** included in the cumulative balance for determining if the mortgage application is downgraded to a Refer.



## **Non-Derogatory Disputed Accounts and Disputed Accounts Not Indicated on the Credit Report**

Non-Derogatory Disputed Accounts include the following types of accounts:

- Disputed accounts with zero balance;
- Disputed accounts with late payments aged 24 months or greater; **and**
- Disputed accounts that are current and paid as agreed.



## **Non-Derogatory Disputed Accounts and Disputed Accounts Not Indicated on the Credit Report (cont.)**

Non-Derogatory Disputed Accounts the Mortgagee:

- Is not required to downgrade the application to a Refer;
- Must analyze the effect of the disputed accounts on the Borrower's ability to repay the mortgage; and
- Must provide acceptable documentation from the borrower if the the dispute results in the Borrower's monthly debt payments utilized in computing the Debt-to-Income (DTI) ratio being less than the amount indicated on the credit report.



## Non-Derogatory Disputed Accounts and Disputed Accounts Not Indicated on the Credit Report (cont.)

- Non-derogatory disputed accounts are **excluded** from the \$1,000 cumulative balance.



# Judgments

- **Judgment** refers to any debt or monetary liability of the Borrower, and the Borrower's spouse in a community property state unless excluded by state law, created by a court, or other adjudicating body.
- The Mortgagee must verify that court-ordered Judgments are resolved or paid off prior to or at closing.





# Judgments: Exception Policy Clarification

## Exception:

A Judgment is considered resolved if the Borrower has:

- entered into a valid agreement with the creditor to make regular payments on the debt;
  - has made timely payments for at least three months of scheduled payments; and
  - the Judgment will not supersede the FHA-insured mortgage lien.
- The Borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments.

*Note: All judgment liens must be subordinated.*



## Judgments: Payment Agreement

The Mortgagee must:

- Include the payment amount in the agreement in the Borrower's monthly liabilities and debt;
- Obtain a copy of the agreement;
- Evidence for at least three months that payments were made on time in accordance with the agreement; and
- Include the subordination agreement for any liens existing on title.



## Inaccuracy in Debt Considered

When an inaccuracy in the amount or type of debt or obligation is revealed during the application process and the correct information was **not considered by the AUS**, the Mortgagee must:

- **Verify** the actual monthly payment amount;
- **Re-submit** the mortgage for evaluation by TOTAL if the cumulative change in the amount of the liabilities that must be included in the Borrower's debt **increases by more than \$100 per month; and**
- **Determine that the additional debt was not/will not** be used for the Borrower's Minimum Required Investment (MRI).



## Bankruptcy: Discharge Period

- The Mortgagee must document the passage of two years since the discharge date of any bankruptcy.
- If the bankruptcy was discharged within two years from the date of case number assignment, the mortgage must be downgraded to a Refer and manually underwritten.



## Pre-Foreclosure Sales (Short Sales) Definition:

- **Short Sale**: Refers to any sale of real estate that generates proceeds that are less than the amount owed on the property and the lien holders agree to release their liens and forgive the deficiency balance on the real estate.



## Short Sale: Period

- The Mortgagee must document the passage of three years since the date of the short sale. If the short sale occurred within three years of the case number assignment date, the mortgage must be downgraded to a Refer and manually underwritten.
- If the credit report does not verify the date of the transfer of title by short sale, the Mortgagee must obtain the short sale documents. A Borrower is generally not eligible for a new FHA-insured mortgage if they relinquished a property through a short sale within three years from the date of case number assignment.
- This three-year period begins on the date of transfer of title by short sale.



# Foreclosure

- The Mortgagee must manually downgrade to a Refer if the Borrower had a foreclosure in which title transferred from the Borrower within three years of case number assignment.
- If the credit report does not verify the date of the transfer of title through the foreclosure, the Mortgagee must obtain the foreclosure documents.



## Deed-in-Lieu (DIL) of Foreclosure

- The Mortgagee must manually downgrade to a Refer if the Borrower had a DIL of foreclosure in which title transferred from the Borrower within three years of case number assignment.
- If the credit report does not verify the date of the transfer of title by DIL of foreclosure, the Mortgagee must obtain a copy of the DIL of foreclosure.





## Credit Counseling/Payment Plan

- Participating in a consumer credit counseling program does not require a downgrade to a manual underwriting.
- No explanation or other documentation is needed.



# Housing Obligation/Mortgage Payment History

- A Housing Obligation/Mortgage Payment refers to the monthly payment due for rental or properties owned.
- A Mortgage Payment is considered delinquent if **not paid within the month due**.
- A mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



# Mortgage Payment Downgrade: Obligations/Mortgage Payment History Purchase and No Cash-Out Refinance Transactions

## Purchase and No Cash-Out Refinance Transactions

Downgraded to a Refer if any mortgage trade line reflects:

Most recent 12 months

$\geq 3 \times 30$

Three or more late payments of greater than 30 Days

$\geq 1 \times 60 + \geq 1 \times 30$

One or more late payments of 60 Days plus one or more 30 Day late payments.

$\geq 1 \times 90$

One payment greater than 90 Days late.

\* A Mortgage Payment is considered delinquent if not paid within the month due.

\*\* Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



# Mortgage Payment Downgrade: Obligations/ Mortgage Payment History Cash-Out Refinance Transactions

## Cash-Out Refinance Transactions

Downgraded to a Refer if any mortgage trade line reflects:

- Any delinquency within 12 months of the case assignment date; and/or
- A current delinquency.

\*A Mortgage Payment is considered delinquent if not paid within the month due.

\*\*Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



## Timeshare: Evaluation of Payment History

If a loan is secured by a Timeshare and the trade line is identified as:

- A mortgage for a TOTAL underwrite the trade line must be evaluated as a mortgage.
- An installment debt for a TOTAL underwrite the trade line is evaluated as an installment debt.



# Evaluating Liabilities and Debts



# Inquiries

- The Mortgagee must review all credit report inquiries to ensure that all debts, including any new debt payments resulting from **material inquiries** listed on the credit report, are used to calculate the debt ratios.
- The Mortgagee must also determine that any recent debts were not incurred to obtain any part of the borrower's required funds to close on the property being purchased.
- **Material Inquiries** refer to inquiries that may potentially result in obligations incurred by the Borrower for other mortgages, auto loans, leases, or other Installment Loans.
- Inquiries from department stores, credit bureaus, and insurance companies are not considered material inquiries.



## Closed-end Debts Paid Off Within 10 Months

- Closed-end debts do not have to be included if:
  - They will be paid off within 10 months; and
  - The cumulative payments of all such debts are less than or equal to 5 percent of the Borrower's gross monthly income.
- The Borrower may not pay down the balance in order to meet the 10-month requirement.





## Authorized User Accounts

Accounts for which the Borrower is an authorized user must be included in a Borrower's DTI ratio unless the Mortgagee can obtain documentation to evidence:

- The primary account holder has made all the required payments on the account for the previous 12 months.
- If less than three payments have been required on the account in the previous 12 months, the payment amount must be included in the Borrower's DTI.



# Undisclosed Debt Other Than a Mortgage

- When a debt or obligation (other than a mortgage) not listed on the mortgage application and/or credit report and not considered by the AUS is revealed during the application process, the Mortgagee must:
  - Verify the actual monthly payment amount;
  - Re-submit the mortgage for evaluation by TOTAL if the cumulative change in the amount of the liabilities that must be included in the Borrower's debt increases by more than \$100 per month; **and**
  - Determine that any funds borrowed were not/will not be used for the Borrower's MRI (Minimum Required Investment).



# Undisclosed Mortgage

- When a debt or obligation that is secured by a mortgage not listed on the mortgage application and/or credit report and not considered by the AUS is revealed during the application process, the Mortgagee must downgrade to a Refer and manually underwrite the mortgage.



# Alimony, Child Support, or Other Maintenance

- For alimony, if the Borrower's income was not reduced by the amount of the monthly alimony obligation in the Mortgagee's calculation of the Borrower's gross income, the Mortgagee must verify and include the monthly obligation in its calculation of the Borrower's debt.
- Child support and other maintenance are to be treated as a recurring liability and the Mortgagee must include the monthly obligation in the Borrower's liabilities and debt.
- The Mortgagee must calculate the Borrower's monthly obligation from the greater of:
  - The amount shown on the most recent decree or agreement establishing the Borrower's payment obligation; or
  - The monthly amount of the garnishment.



## Alimony, Child Support, or Other Maintenance (cont.)

- The Mortgagee must obtain the official signed divorce decree, separation agreement, maintenance agreement, or other legal order.
- The Mortgagee must also obtain the Borrower's pay stubs covering no less than **28 consecutive Days** to verify whether the Borrower is subject to any order of garnishment relating to the alimony, child support, or other maintenance.
- The Mortgagee must calculate the Borrower's monthly obligation from the greater of:
  - The amount shown on the most recent decree or agreement establishing the Borrower's payment obligation; or
  - The monthly amount of the garnishment.



## Deferred Obligations: Clarification

- **Deferred Obligations** refer to liabilities that have been incurred but where payment is deferred or has not yet commenced, including accounts **in forbearance**.
- The Mortgagee must verify and include deferred obligations in the calculation of the Borrower's debt.



## Deferred Obligations: Clarification (cont.)

Mortgagee must use the actual monthly payment to be paid on a deferred liability, whenever available.

If the actual monthly payment is not available, for:

- **Installment Debt:**
  - 5 percent of the outstanding balance to establish the monthly payment.
- **Student Loan:**
  - 2 percent of the outstanding balance to establish the monthly payment.



# Installment Loans

- **Installment Loans** refer to loans, not secured by real estate, that require the periodic payment of principal and interest.
- The Mortgagee must include the monthly payment shown on the credit report, loan agreement, or payment statement to calculate the Borrower's debts.





# Installment Loan Monthly Payment Clarification

- If the credit report does not include a monthly payment for the loan, the Mortgagee must use the amount of the monthly payment shown in the loan agreement or payment statement and enter it into TOTAL Mortgage Scorecard.
- If the monthly payment shown on the credit report is utilized to calculate the monthly debts, no further documentation is required.
- If the credit report does not include a monthly payment for the loan, or the payment reported on the credit report is greater than the payment on the loan agreement or payment statement, the Mortgagee must obtain a copy of the loan agreement or payment statement documenting the amount of the monthly payment.



## Revolving Charge Accounts: Documentation

- The Mortgagee must use the credit report to document the terms, balance, and payment amount on the account, if available.
- Where the credit report does not reflect the necessary information on the charge account, the Mortgagee must:
  - Obtain a copy of the most recent charge account statement; or
  - Use **5 percent** of the outstanding balance to document the monthly payment.



## 30-Day Accounts

- **30-Day Accounts** refer to a credit arrangement that requires the Borrower to pay-off the outstanding balance on the account every month.
- The Mortgagee must verify the Borrower paid the outstanding balance in full on every 30-Day Account each month for the past 12 months.



## 30-Day Accounts (cont.)

- 30-Day Accounts that are paid monthly on time for the past 12 months are not included in the Borrower's DTI.
- If the credit report reflects any late payments in the last 12 months, the Mortgagee must utilize 5 percent of the outstanding balance as the Borrower's monthly debt to be included in the DTI.



# Contingent Liabilities

- A **Contingent Liability** refers to a liability that may result in the obligation to repay only when a specific event occurs.
- For example, a contingent liability exists when an individual can be held responsible for the repayment of a debt if another legally obligated party defaults on the payment.
- Contingent liabilities may include cosigner liabilities and liabilities resulting from a mortgage assumption without release of liability.



## Contingent Liabilities (cont.)

- The Mortgagee must include monthly payments on contingent liabilities in the calculation of the Borrower's monthly obligations **unless** the Mortgagee verifies and documents that there is **no possibility** that the **debt holder will pursue debt collection against the Borrower** should the other party default or the other legally obligated party **has made 12 months of timely payments**.
- The Mortgagee must calculate the monthly payment on the contingent liability based on the terms of the agreement creating the contingent liability.



# Contingent Liabilities: Mortgage Assumptions

- The Mortgagee must obtain the agreement creating the contingent liability or assumption agreement and deed showing transfer of title out of the Borrower's name.

*Note: The Mortgagee verifies and must document that there is **no possibility** that the **debt holder will pursue debt collection against the Borrower** should the other party default.*



## Contingent Liabilities: Cosigned Liabilities

- If the cosigned liability is **not included** in the monthly obligation, the Mortgagee must obtain documentation to evidence that the other party to the debt has been making regular on-time payments during the previous 12 months, and does not have a history of delinquent payments on the loan.





## Contingent Liabilities: Divorce

- The Mortgagee must obtain a copy of the divorce decree ordering the spouse to make payments.



## Collection Accounts

- A **Collection Account** refers to a Borrower's loan or debt that has been submitted to a collection agency by a creditor.
- Medical Collections, are not required to be paid, satisfied, or considered in the Borrower's qualifying ratios.



## Collection Accounts (cont.)

If the credit reports used in the analysis show a **cumulative outstanding collection account balances of \$2,000 or greater**, the Mortgagee must:

- Verify that the debt is paid in full at the time of or prior to settlement using an acceptable source of funds;
- Verify that the Borrower has made payment arrangements with the creditor and include the monthly payment in the Borrower's DIT; or
- If a payment arrangement is not available, calculate the monthly payment using 5 percent of the outstanding balance of each collection and include the monthly payment in the Borrower's DTI ratio.



## Collection Accounts (cont.)

- Collection accounts of a non-borrowing spouse in a community property state must be included in the \$2,000 cumulative balance and analyzed as part of the Borrower's ability to pay all collection accounts, unless specifically excluded by state law.
- The Mortgagee must provide the following documentation:
  - Evidence of payment in full, if paid prior to settlement; or
  - The payoff statement, if paid at settlement; or
  - The payment arrangement with creditor, if not paid prior to or at settlement.
- If the Mortgagee uses **5 percent** of the outstanding balance, no documentation is required.



## Charge Off Accounts

- A **Charge Off Account** refers to a Borrower's loan or debt that has been written off by the creditor.
- Charge off accounts **do not** need to be included in the Borrower's liabilities or debt.



# Private Savings Clubs

- **Private Savings Club** refers to a non-traditional method of saving by making deposits into a member-managed resource pool.
- If the Borrower is obligated to continue making ongoing contributions under the pooled savings agreement, **this obligation must be counted in the Borrower's total debt.**
- The Mortgagee must verify and document the establishment and duration of the Borrower's membership in the club and the amount of the Borrower's required contribution to the club.
- The Mortgagee must also obtain the club's account ledgers and receipts, and verification from the club treasurer that the club is still active.



## Private Savings Clubs (cont.)

- Under this situation, if the Borrower is obligated to continue making ongoing contributions under the pooled savings agreement, **this obligation must be counted in the Borrower's total debt.**
- **How would the Mortgagee enter this identify this account?**



## Private Savings Clubs (cont.)

- **How would the Mortgagee enter this identify this account?**
- The Mortgagee needs to identify the monthly obligation as a monthly liability in the Borrower's DTI and verify that there AUS has identified this account in its transmission to TOTAL.





## Business Debt in Borrower's Name

- When a self-employed Borrower states debt appearing on their personal credit report is being paid by their business, the Mortgagee must obtain documentation to evidence the following:



## Business Debt in Borrower's Name (cont.)

- The company has been making regular on-time payments during the previous **12 months without delinquency**;
- The debt is paid out of company funds; **and**
- The debt was considered in the cash-flow analysis of the Borrower's business.



# Business Debt Considered in Cash Flow Analysis

- When the personal Borrower's debt is being paid by the Borrower's business, then is considered:
  - In the cash flow analysis and the Borrower's business tax returns reflect a business expense related to the obligation, equal to or greater than the amount of payments documented as paid out of company funds,
  - the Borrower's business tax returns may show an interest expense related to the obligation, **only the interest portion of the debt can be considered in the cash flow analysis.**



# Negative Income

- Negative income must be subtracted from the Borrower's gross monthly income, and not treated as a recurring monthly liability unless otherwise noted.



## Source of Funds for Debts Paid Prior to Close

- The Mortgagee must document that the funds used to pay off debts prior to closing came from an acceptable source, and the Borrower did not incur new debts that were not included in the DTI ratio.



# Obligations Not Considered Debt

- Medical collections
- Federal, state, and local taxes, if not delinquent and no payments are required
- Automatic deductions from savings, when not associated with another type of obligation
- Federal Insurance Contributions Act (FICA) and other retirement contributions, such as 401(k) accounts
- Collateralized loans secured by depository accounts
- Utilities
- Child care
- Commuting costs
- Union dues
- Insurance, other than property insurance
- Open accounts with zero balances
- Voluntary deductions, when not associated with another type of obligation



# Income Requirements



# Feedback Certification: General Income Requirements

- As we have discussed, the Mortgagee must review the Feedback Certificate for accuracy and validate the data provided for TOTAL's risk evaluation.





## Feedback Certification: General Income Requirements (cont.)

The Mortgagee must:

- Document the Borrower's income;
- Document employment history;
- Verify the accuracy of the amounts of income being reported;  
**and**
- Determine if the income can be considered as Effective Income.



# General Income Requirements

- **Effective Income** refers to income that may be used to qualify a Borrower for a mortgage.
- **Effective Income** must:
  - Be likely to continue through at least the first three years of the mortgage;
  - Be documentable;
  - Be legally derived;
  - Be reported to the IRS when required; and
  - Subtract negative income from the Borrower's gross monthly income.



## Employment Related Income

- **Employment Income** refers to income received as an employee of a business that is reported on IRS Form W-2.
- The Mortgagee may use Employment-related Income as Effective Income in accordance with the standards provided for each type of Employment-related Income.



## Employment Related Income (cont.)

- For all Employment related Income, the Mortgagee must verify the Borrower's most recent two years of employment and income, and document using one of the following methods:
  - Traditional Current Employment Documentation; or
  - Alternative Current Employment Documentation.



## Traditional Current Employment Documentation

- To verify the borrowers current employment, the Mortgagee must obtain:
  - The most recent pay stub; **and**
  - A written Verification of Employment (VOE) or an electronic verification acceptable to FHA covering the most recent two years.



# Alternative Current Employment Documentation

- To verify the borrowers **current employment**, the Mortgagee must obtain:
  - Copies of the most recent pay stub that shows the Borrower's year-to-date earnings;
  - Copies of the original IRS W-2 forms from the previous two years; **and a**
  - Telephone employment certification
    - Document current employment by telephone, sign and date the verification documentation, and note the name, title, and telephone number of the person with whom employment was verified.



## Re-verification of Employment

- Re-verification of employment must be completed within 10 Days prior to the date of the Note.
- Verbal re-verification of employment is acceptable.



## Past Employment Documentation: Current Employment for Two Years

- Direct verification of the Borrower's employment history for the previous two years is not required if **all** of the following conditions are met:
  - The current employer confirms a two-year employment history, or a paystub reflects a hiring date of a minimum of two years;
  - Only **base pay** is used to qualify (no Overtime or Bonus Income); **and**
  - The Borrower executes IRS Form 4506, *Request for Copy of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, for the previous two tax years.





## Past Employment Documentation: Current Employment Less Than Two Years (cont.)

- If the Borrower has not been employed with the same employer for the previous two years and/or not all conditions previously discussed are not able to be met (**Counting Overtime/Bonus**), then the Mortgagee must **obtain one or a combination** of the following for the **most recent two years** to verify the applicant's employment history:
  - W-2(s);
  - VOE(s);
  - Electronic verification acceptable to FHA; and
  - Evidence supporting enrollment in school or the military during the most recent two full years.



# Primary Employment

- Primary Employment is the Borrower's principal employment. Primary Employment is generally full-time employment.
- The Mortgagee may use primary employment income as Effective Income.



## Calculation of Effective Income: Salary

- **Salary** refers to Income that has been and will likely be consistently earned, the Mortgagee must use the current salary to calculate the Effective income.



## Calculation of Effective Income: Hourly

- **Hourly Wage Earners whose:**
  - **Hours do not vary**, the Mortgagee must consider the Borrower's current hourly rate to calculate Effective Income.
  - **Hours vary**, the Mortgagee must average the income over the previous two years.
- If the Mortgagee can **document an increase in pay rate**, the Mortgagee may use the most recent 12-month average of hours at the current pay rate.



# Overtime and Bonus Income

- **Overtime and Bonus Income** refers to income that the Borrower receives in addition to the Borrower's normal salary.



## Overtime and Bonus Income

- The Mortgagee may use Overtime and Bonus Income as Effective Income if the Borrower has received this income for the **past two years** and it is **reasonably likely to continue**.
- Periods of Overtime and Bonus Income **less than two years** may be considered Effective Income if the Mortgagee documents that the Overtime and Bonus Income has been consistently earned over a period of **not less than one year** and is **reasonably likely to continue**.



# Overtime and Bonus Income: Calculation

## Calculation:

- The Mortgagee must average the Overtime or Bonus Income over the previous two years.
- However, if the Overtime or Bonus Income from the current year **decreases by 20% or more** from the previous, the Mortgagee must use the current year's income.



# Seasonal Employment

- **Seasonal Employment** refers to employment that is not year round, regardless of the number of hours per week the Borrower works on the job.





## Seasonal Employment

- The Mortgagee may consider Seasonal Employment income as Effective Income if the Borrower:
  - Has worked the same line of work for the past two years;  
**and**
  - Is reasonably likely to be rehired for the next season.
- The Mortgagee may consider unemployment income as Effective Income for those with effective Seasonal Employment income.



# Seasonal Employment

## Calculation of Effective Income:

- For employees with Seasonal Employment income, the Mortgagee must average the income earned over the previous two full years to calculate Effective Income.
- For seasonal employees with unemployment income, the Mortgagee must document the **unemployment income for two full years** and there must be reasonable assurance that this income will continue.



## Employed by Family-Owned Business

- The Mortgagee may consider Family-Owned Business Income as Effective Income if the Borrower is not an owner in the family-owned business.
- The Mortgagee must verify and document that the **Borrower is not an owner in the family-owned business by using official business documents showing the ownership percentage.**



## Employed by Family-Owned Business (cont.)

- Official business documents include:
  - Corporate resolutions or other business organizational documents;
  - Business tax returns or Schedule K-1(IRS Form 1065), U.S. Return of Partnership Income; **or**
  - An official letter from a certified public accountant on their business letterhead.
- In addition to traditional or alternative documentation requirements, the Mortgagee must obtain copies of signed personal tax returns or tax transcripts.



## Commission Income

- **Commission Income** refers to income that is paid contingent upon the conducting of a business transaction or the performance of a service.
- The Mortgagee may use Commission Income as Effective Income if:
  - The Borrower earned the **income for at least one year in the same or similar line of work**; and
  - It is reasonably likely to continue.



## Commission Income: Documentation

- **Commission Income less than or equal to 25%** of the Borrower's total earnings, the Mortgagee must use traditional or alternative employment documentation.
- **Commission Income greater than 25%** of the Borrower's total earnings, the Mortgagee must obtain signed tax returns, including all application schedules, for the last two years.
- In lieu of signed tax returns from the Borrower, the Mortgagee may obtain a signed IRS Form 4506, Request for Copy of Tax Return, IRS Form 4506-T, Request for Transcript of Tax Return, or IRS Form 8821, Tax Information Authorization, and tax transcripts directly from the IRS.



## Self-Employment Income

- **Self-Employment Income** refers to income generated by a business in which the Borrower has a 25 percent or greater ownership interest.
- The Mortgagee may consider Self-Employment Income if the Borrower has been self-employed **for at least two years**.
- If the Borrower has been self-employed between **one and two years**, the Mortgagee may only consider the income as Effective Income if the Borrower was previously employed in the same line of work in which the Borrower is self-employed or in a related occupation for at least two years.



## Self-Employment Income: Stability

- Income obtained from businesses with **annual earnings that are stable or increasing is acceptable.**
- If the income from businesses shows a greater than 20 percent decline in Effective Income over the analysis period, the Mortgagee **must downgrade the transaction to a Refer and manually underwrite the transaction.**





# Self-Employment Income: Documentation

- **Individual and Business Tax Returns**
  - The Mortgagee must obtain complete individual and business federal income tax returns for the most recent two years, including all schedules.
  - **In lieu of signed individual or business tax returns from the Borrower**, the Mortgagee may obtain a signed IRS Form 4506, Request for Copy of Tax Return, IRS Form 4506-T, Request for Transcript of Tax Return, or IRS Form 8821, Tax Information Authorization, and tax transcripts directly from the IRS.



## Self-Employment Income-Documentation (cont.)

- The Mortgagee must obtain the Borrower's business tax returns for the most recent two years **unless** the following criteria are met:
  - Individual federal income tax returns show **increasing** Self-Employment Income over the past two years;
  - **Funds to close** are not coming from **business accounts**; and
  - The mortgage to be insured is **not a cash-out refinance**.



## Self-Employment Income-Documentation (cont.)

- The Mortgagee must obtain a year-to-date Profit and Loss (P&L) statement and balance sheet if:
  - More than a calendar quarter has elapsed since date of most recent calendar or fiscal year-end tax return was filed by the Borrower.
- A balance sheet is **not required** for self-employed Borrowers filing **Schedule C income**.
- If **income used to qualify** the Borrower **exceeds the two year average of tax returns**, an **audited P&L or signed quarterly tax return must be obtained from the IRS**.



## Self-Employment Income: Calculation

- The Mortgagee must calculate gross Self-Employment Income by using the lesser of:
  - The average gross Self-Employment Income earned over the previous two years; or
  - The average gross Self-Employment Income earned over the previous one year.



## Frequent Changes in Employment

- If the Borrower has changed jobs more than **three times** in the **previous 12-month** period, or has changed lines of work, the Mortgagee must take additional steps to verify and document the stability of the Borrower's Employment Income.
- The Mortgagee must obtain:
  - Transcripts of training and education demonstrating qualification for a new position; **or**
  - Employment documentation evidencing continual increases in income and/or benefits.



## Gaps in Employment

- For Borrowers with gaps in employment of six months or more (an extended absence), the Mortgagee may consider the Borrower's current income as Effective Income if it can verify and document that:
  - The Borrower has been employed in the current job for at least six months at the time of case number assignment;  
**and**
  - A two year work history prior to the absence from employment using standard or alternative employment verification.



## Temporary Reduction in Income

- For Borrowers with a temporary reduction of income due to a short-term disability or similar temporary leave, the Mortgagee may consider the Borrower's current income as Effective Income, if it can verify and document that:
  - The Borrower **intends** to return to work;
  - The Borrower **has the right** to return to work; and
  - The Borrower **qualifies** for the mortgage taking into account any **reduction of income** due to the circumstance.



## Temporary Reduction in Income: Calculation

- Borrowers returning to work before or at the time the first Mortgage Payment due date; **and**
- The Mortgagee may use the Borrower's pre-leave income.





## Temporary Reduction in Income: Calculation (cont.)

**Borrowers returning to work *after* the first Mortgage Payment due date:**

- The Mortgagee may use the Borrower's current income plus available surplus liquid asset Reserves, above and beyond any required Reserves, as an income supplement up to the amount of the Borrower's pre-leave income.
- The amount of the monthly income supplement is:
  - The total amount of **surplus Reserves divided by the number of months between the first payment due date and the Borrower's intended date of return to work.**
- ***Surplus Liquid Asset Reserves:*** Liquid asset reserves above and beyond the program requirements.



# Temporary Reduction in Income: Documentation

The Mortgagee must provide the following **documentation** for Borrowers on temporary leave:

- A written statement from the Borrower confirming the Borrower's intent to return to work, and the intended date of return;
- Documentation generated by current employer confirming the Borrower's eligibility to return to current employer after temporary leave; and
- Documentation of sufficient liquid assets, to be used to **supplement the Borrower's income** through the intended return date to work after the first due date of the mortgage payment.



## Case Study: Maternity Leave

Lisa and Jim Smith have applied for a FHA purchase 203(b) mortgage. At the time of underwriting, Ms. Smith is on Maternity leave from her position. The following information is in the case file:

- A written statement from Ms. Smith verifying her intentions to return to her full-time position.
- A Verification of Employment from Ms. Smith's employer stating ;
  - Ms. Smith is on Temporary Leave without pay.
  - Ms. Smith's position is being retained for her.
  - Upon her return she will be paid at the same salary rate of \$28,000/year.
  - Ms. Smith has held her salaried position for the last 12 years.
- It is Ms. Smith's intent to be returning back to work 1 month after the due date of the first mortgage payment.
- The Smith's total Surplus Liquid Asset Reserves are \$1100.



## Case Study: Maternity Leave

What is Ms. Smith's Effective Income?

- It is Ms. Smith's intent to be returning back to work 1 month after the due date of the first mortgage payment.
- The Smith's total Surplus Liquid Asset Reserves are \$1100.

Ms. Smith's Effective Income is \$1100.

- Ms. Smith currently is not making any income. The only Effective Income source is the Surplus Liquid Asset Reserves.
- "The Mortgagee may use the Borrower's current income plus available surplus liquid asset Reserves, above and beyond any required Reserves, as an income supplement up to the amount of the Borrower's pre-leave income."



## Alimony, Child Support, or Maintenance Income

- **Alimony, Child Support, or Maintenance Income** refers to income received from a former spouse or partner or from a non-custodial parent of the Borrower's minor dependent.



## **Alimony, Child Support, or Maintenance Income (cont.)**

- The Mortgagee must obtain a fully executed copy of the Borrower's final divorce decree, legal separation agreement, court order, or voluntary payment agreement with documented receipt.
- The Mortgagee may use the front and pertinent pages of the divorce decree/settlement agreement and/or court order showing the financial details.



# Alimony, Child Support or Maintenance Income: Legal Record - Documentation

- When using a final divorce decree, legal separation agreement, or court order, the Mortgagee must obtain evidence of receipt using the following documentation for the **most recent three months** that supports the amount used in qualifying:
  - Deposits on bank statements;
  - Canceled checks; or
  - Documentation from the child support agency.
- The Mortgagee must provide evidence that the claimed income will continue for at least three years.



## Alimony, Child Support, or Maintenance Income: Legal Record - Effective Income

- When using a final divorce decree, legal separation agreement, or court order, if the Borrower has received **consistent** Alimony, Child Support or Other Maintenance payments for the **most recent three months**, the Mortgagee may use the **current payment to calculate Effective Income**.





# Alimony, Child Support or Maintenance Income: Voluntary - Documentation

- The Mortgagee must document the voluntary payment agreement with:
  - 12 months of cancelled checks,
  - Deposit slips, **or**
  - Tax returns.
- The Mortgagee must provide evidence that the claimed income will continue for at least three years.



## **Alimony, Child Support, or Maintenance Income: Voluntary – Effective Income**

- When using evidence of voluntary payments, if the Borrower has received consistent alimony, child support or other maintenance payments for the most recent six months, the Mortgagee may use the current payment to calculate Effective Income.



## Alimony, Child Support, or Maintenance Income: Inconsistent Payments– Effective Income

- If **legal record or voluntary payment** alimony, child support, or other maintenance payments **have not been consistently received** for the **most recent six months**, the Mortgagee must use the **average of the income received over the previous two years** to calculate Effective Income.
- If Alimony, Child Support, or Maintenance Income has been received **for less than two years**, the Mortgagee must **use the average over the time of receipt**.



# Military Income: Expiration Term of Service Date

- The Mortgagee must:
  - Obtain a copy of the Borrower's military Leave and Earnings Statement (LES); and
  - Verify **the Expiration Term of Service date** on the LES.
- If the Expiration Term of Service date is **within the first 12 months of the mortgage**, Military Income may only be considered Effective Income if the **Borrower represents their intent to continue military service.**



# Other Public Assistance

## Required Documentation:

- Mortgagees must verify and document the income received from the government agency.
- If any Public Assistance income is due to expire within three years from the date of mortgage application, that income cannot be used as Effective Income.
- If the documentation does not have a defined expiration date, the Mortgagee may consider the income effective and reasonably likely to continue.



# Automobile Allowances

- **Automobile Allowance** refers to the funds provided by the Borrower's employer for automobile-related expenses.



## Automobile Allowances: Documentation

The Mortgagee must:

- Verify and document that the Automobile Allowance has been received for the **previous two years**; and
- Obtain IRS Form 2106, Employee Business Expenses, for the last two years.

*Note: Look for “Unreimbursed Employee Expenses”.*



## Automobile Allowances: Calculation

- The Mortgagee must subtract automobile expenses as shown on IRS Form 2106 from the Automobile Allowance before calculating Effective Income based on the current amount of the allowance received.





## Automobile Allowances: Calculation (cont.)

- If the Borrower uses the **standard per-mile rate** in calculating automobile expenses, opposed to the actual cost method, the portion that the IRS considers **depreciation may be added back to income**.



## Automobile Allowances: Calculation (cont.)

- Expenses that must be treated as recurring debt include:
  - The Borrower's monthly car payment; and
  - Any loss resulting from the calculation of the difference between the actual expenditures and the expense account allowance.



# Rental Income

- **Rental Income** refers to income received or to be received from the subject property or other real estate holdings.



# Self-Sufficiency Rental Income Eligibility (Three-to-Four Unit Properties)

- **Net Self-Sufficiency Rental Income** refers to the Rental Income produced by the subject Property over and above the Principal, Interest, Taxes, and Insurance (PITI).
- The PITI divided by the monthly Net Self-Sufficiency Rental Income may not exceed 100 percent for three- to four-unit Properties.
- Net Self-Sufficiency Rental Income is calculated by using the Appraiser's estimate of fair market rent from all units, including the unit the Borrower chooses for occupancy, and **subtracting the greater of the Appraiser's estimate for vacancies and maintenance, or 25 percent of the fair market rent.**



## Rental Income Received from the Subject Property

- How to begin to evaluate Rental Income:
  - Is the rental income being received from the subject property?
  - Does the Borrower have a history of receiving rental income from the subject since the previous tax filing?
  - How long has the Borrower owned the property?



# Limited/No History of Rental Income Received: Subject Property

Borrower Does Not Have a History of Rental Income from the Subject:	One Unit	Two-to-Four Units
	Fannie Mae Form 1004/Freddie Mac Form 70, <i>Uniform Residential Appraisal Report</i> , Fannie Mae Form 1007/Freddie Mac Form 1000, <i>Single Family Comparable Rent Schedule</i> , and Fannie Mae Form 216/Freddie Mac Form 998, <i>Operating Income Statement</i> , showing fair market rent	Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, <i>Small Residential Income Property Appraisal Report</i> )
	The prospective executed lease , if available	The prospective executed leases , if available
Document the date of acquisition by providing the deed, Settlement Statement or other legal document.		



## Limited/No History of Rental Income Received Subject Property: Calculation

- The Mortgagee must **add the net** subject property **Rental Income** to the Borrower's **gross income**.
- The Mortgagee must use the **lesser of**:
  - The monthly operating income reported on Freddie Mac Form 998; **or**
  - 75 percent of the **lesser of**:
    - Fair market rent reported by the appraiser; **or**
    - The rent reflected in the lease or other rental agreement.



# History of Rental Income Received Subject Property

The Borrower has a history of Rental Income from the subject since the previous tax filing:	One Unit	Two-to-Four Units
	Executed lease	Executed leases
	24 month rental history free of unexplained gaps > 3 months	24 month rental history free of unexplained gaps > 3 months
	Borrower's most recent 2 years Tax Returns including Schedule E	Borrower's most recent 2 years Tax Returns including Schedule E
	Properties with less than 2 years of Rental Income history, the date of acquisition must be documented by providing the deed, Settlement Statement or other legal document.	

Note: If rental history over the previous 24 months reflects gaps greater than 3 months, an explanation is required. Such vacancies could be explained by seasonal or military renters, or property rehabilitation.





# History of Rental Income Received Subject Property: Calculation

The Mortgagee must:

- **Add the net** subject property **Rental Income** to the Borrower's **gross income**; and
- Calculate the Rental Income by **averaging** the **amount shown on the Schedule E**.
- The Mortgagee **may not reduce** the Borrower's total **Mortgage Payment** by the net subject property **Rental Income**.
- If the property has been **owned for less than two years**, the Mortgagee must **annualize the Rental Income** for the **length of time the property has been owned**.



## History of Rental Income Received Subject Property: Calculation (cont.)

The following items shown on the Schedule E may be added back to the income or loss:

- Depreciation;
- Mortgage interest;
- Taxes;
- Insurance; and
- any HOA dues.



# Rental Income Received from Other Real Estate Holdings

How to begin to evaluate Rental Income from other real estate holdings:

- Is the rental income being derived from the property being vacated by the Borrower?
- Does the Borrower have a history of receiving rental income from the subject since the previous tax filing?
- How long has the Borrower owned the property?



# Rental Income:

## Property Being Vacated by the Borrower

Rental Income from the Property being Vacated by the Borrower:	One Unit	Two-to-Four Units
	Fannie Mae Form 1004/Freddie Mac Form 70, <i>Uniform Residential Appraisal Report</i> , Fannie Mae Form 1007/Freddie Mac Form 1000, <i>Single Family Comparable Rent Schedule</i> , and Fannie Mae Form 216/Freddie Mac Form 998, <i>Operating Income Statement</i> , showing fair market rent must be obtained on property being vacated. Appraisal not required to be completed by an FHA appraiser.	Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, <i>Small Residential Income Property Appraisal Report</i> ) must be obtained on property being vacated. Appraisal not required to be completed by an FHA appraiser.
	Minimum 25% equity in vacated property	Minimum 25% equity in vacated property
	Executed 1 year lease agreement, commencing after the closing	Executed 1 year lease agreement, commencing after the closing
	Evidence of payment of the security deposit or first month's rent of least agreement.	Evidence of payment of the security deposit or first month's rent of least agreement.
	Evidence that the Borrower is relocating to an area more than 100 miles from the Borrower's current Principal Residence.	



# Rental Income: Limited/No History Other Real Estate

Rental income Limited or No History by the Borrower:	One Unit	Two-to-Four Units
	Fannie Mae Form 1004/Freddie Mac Form 70, <i>Uniform Residential Appraisal Report</i> , Fannie Mae Form 1007/Freddie Mac Form 1000, <i>Single Family Comparable Rent Schedule</i> , and Fannie Mae Form 216/Freddie Mac Form 998, <i>Operating Income Statement</i> , showing fair market rent must be obtained on the investment property (s). Appraisal is not required to be completed by an FHA appraiser.	Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, <i>Small Residential Income Property Appraisal Report</i> ) must be obtained on the investment property (s). Appraisal is not required to be completed by an FHA appraiser.
	Investment property (s) must support a minimum 25% equity position	Investment property must support a minimum 25% equity position
	Executed 1 year lease agreement	Executed 1 year lease agreement
	Properties with less than 2 years of Rental Income history, the date of acquisition must be documented by providing the deed, Settlement Statement or other legal document.	



## Limited/No History of Rental Income Received: Calculation

- To calculate the effective net Rental Income from other real estate holdings where the Borrower **does not have a history of Rental Income** since the previous tax filing, the Mortgagee must **deduct** the PITI from the **lesser of**:
  - The monthly operating income reported on Freddie Mac Form 998; **or**
  - 75 percent of the **lesser of**:
    - Fair market rent reported by the appraiser; **or**
    - The rent reflected in the lease or other rental agreement.



# Rental Income: History Other Real Estate

The Borrower has a History of Rental Income Since the Previous Tax Filing:	One Unit	Two-to-Four Units
	Borrower's most recent 2 years executed Tax Returns including Schedule E	Borrower's most recent 2 years executed Tax Returns including Schedule E
	Properties with less than 2 years of Rental Income history, the date of acquisition must be documented by providing the deed, Settlement Statement or other legal document.	



# History of Rental Income Received: Calculation

- The Mortgagee must:
  - Calculate the Rental Income by **averaging** the **amount shown on the Schedule E** provided, the Borrower continues to own all properties included on the Schedule E;
  - Annualize the Rental Income for properties owned less than two year;
  - Add positive Rental Income to the Borrower's Effective income; and
  - Include negative net Rental Income as a reoccurring debt/liability.
- Depreciation shown on Schedule E may be added back to the net income or loss.





## Boarder Income: Purchase Transactions

- **Boarder** refers to an individual renting space inside the Borrower's Dwelling Unit.
- Purchase Transactions:
  - The Mortgagee must obtain **two years of the Borrower's tax returns evidencing income from Boarders and the current lease.**
- For purchase transactions, the Mortgagee must obtain a copy of the executed written agreement documenting their intent to continue boarding with the Borrower.



## Expected Income

- **Expected Income** refers to income from cost-of-living adjustments, performance raises, a new job, or retirement that has not been, but will be received within 60 Days of mortgage closing.



## Expected Income from Family-Owned Business

- The Mortgagee may consider Expected Income as Effective Income except when Expected Income is to be derived from a family-owned business.



## Expected Income: Verification

- The Mortgagee must verify and document that the Borrower will have sufficient income or cash reserves to support the mortgage payment and any other obligations between the mortgage closing and the start of the Expected Income.
- For expected Employment Income, the Mortgagee must verify the existence and **the amount** of the Expected Income with the employer in **writing** and that it is guaranteed to begin within **60 Days** of mortgage closing.
- **For expected Retirement Income**, the Mortgagee must verify **the amount** and that it is **guaranteed** to begin within **60 Days** of the mortgage closing.



## Non-Taxable Income (Grossing Up)

- **Non-Taxable Income** refers to types of income not subject to federal taxes.
- The Mortgagee must document and support:
  - The amount of income to be Grossed Up for any non-taxable income source; and
  - The current tax rate applicable to the Borrower's income that is being Grossed Up.



## Non-Taxable Income (Grossing Up): Calculation

- Non-Taxable Income that may be added cannot exceed the **greater of 15 percent or the appropriate tax rate for the income amount**, based on the Borrower's tax rate for the previous year.
- If the **Borrower was not required to file a federal tax return** for the previous tax reporting period, the Mortgagee may Gross Up the Non-Taxable Income by **15 percent**.
- The Mortgagee may not make any additional adjustments or allowances based on the number of the Borrower's dependents.



# Asset Requirements



## General Asset Requirements

- The Mortgagee may only consider assets derived from acceptable sources in accordance with FHA Single Family Housing Policy.
- Closing costs, prepaid items, and other fees may not be applied towards the Borrower's minimum required investment.





# Earnest Money Deposit

- The Mortgagee must verify and document the deposit amount and source of funds if the amount of the earnest money deposit **exceeds 1 percent** of the sales price or is **excessive based on the Borrower's history of accumulating savings**, by obtaining:
  - A copy of the Borrower's cancelled check;
  - Certification from the deposit-holder acknowledging receipt of funds; **or**
  - A Verification of Deposit (VOD) or bank statement showing that the average balance was sufficient to cover the amount of the earnest money deposit at the time of the deposit.
- If the source of the earnest money deposit was a gift, the Mortgagee must verify that the gift is in compliance with Gifts (Personal and Equity).



## Premium Pricing on FHA-Insured Mortgages

- Premium Pricing refers to a credit from a Mortgagee for the interest rate chosen.
- Premium Pricing may be used to pay a Borrower's actual closing costs and/or prepaid items.
- Closing costs paid in this manner do not need to be included as part of the Interested Party limitation.



## Premium Pricing on FHA-Insured Mortgages (cont.)

- The funds derived from a premium priced mortgage:
  - Must be disclosed in accordance with RESPA;
  - Must be used to reduce the principal balance if the credit amount exceeds the actual dollar amount for closing costs and prepaid expenses; **and**
  - May not be used for payment of debts, collection accounts, escrow shortages, or missed Mortgage Payments, or Judgments.



# Interested Party Contributions on the Settlement Statement

- The Mortgagee may apply Interested Party credits to the origination fees, other closing costs, and discount points, including any items Paid Outside Closing (POC).
- The refund of the Borrower's POCs may be used toward the Borrower's MRI if the Mortgagee documents that the POCs were paid with the Borrower's own funds.
- The Mortgagee must identify each item paid by Interested Party contributions:
  - The total Interested Party credits on the front page of the Settlement Statement or similar legal document or in an addendum.



## Real Estate Tax Credits

- Where real estate taxes are paid in arrears, the seller's real estate tax credit may be used to meet the minimum required investment (MRI), if the Mortgagee documents that the Borrower had sufficient assets to meet the MRI and the Borrower paid closing costs at the time of underwriting.
- This permits the Borrower to bring a portion of their MRI to the closing and combine that portion with the real estate tax credit for their total MRI.



## Reserves

- **Reserves** refer to the sum of the Borrower's verified and documented liquid assets minus the total funds the Borrower is required to pay at closing.
- The Mortgagee must verify and document all assets submitted to the AUS.



## Reserves (cont.)

Reserves do not include:

- The amount of cash taken at settlement in cash-out transactions;
- Incidental cash received at settlement in other loan transactions;
- Equity in another property; or
- Borrowed funds from any source.



## Source Requirements for the Borrower's Minimum Required Investment (MRI)

- **Minimum Required Investment (MRI)** refers to the Borrower's contribution in cash or its equivalent required by Section 203(b)(9) of the National Housing Act, which represents at least 3.5 percent of the **Adjusted Value of the property**.





## Source Requirements for the Borrower's Minimum Required Investment (MRI) (cont.)

- Where the **Borrower's MRI** is provided by someone other than the **Borrower**, the **Mortgagee** must also obtain **documentation** to support the permissible nature of the **source of those funds**.



## Source Requirements for the Borrower's Minimum Required Investment (MRI) (cont.)

- The Mortgagee may only permit the Borrower's MRI to be provided by a source permissible under Section 203(b)(9)(C) of the National Housing Act, which means the funds for the Borrower's MRI **must not** come from:
  - 1) The seller of the property;
  - 2) Any other person or Entity who financially benefits from the transaction (directly or indirectly); or
  - 3) Anyone who is or will be reimbursed, directly or indirectly, by any party included in (1) or (2) above.
- While additional funds to close may be provided by one of these sources if permitted under the relevant source of funds requirements above, **none of the Borrower's MRI may come from these sources.**
- The Mortgagee must document permissible sources for the full MRI in accordance with special requirements noted above.



## Checking and Savings Accounts

- For recently opened accounts and recent individual deposits of more than one percent of the Adjusted Value, the Mortgagee must:
  - Obtain documentation of the deposits; **and**
  - Verify that no debts were incurred to obtain part, or all, of the MRI.



## Standards for Gifts

- Gifts may be provided by:
  - The Borrower's Family Member;
  - The Borrower's employer or labor union;
  - A close friend with a clearly defined and documented interest in the Borrower;
  - A charitable organization; **or**
  - A governmental agency or Public Entity that has a program providing homeownership assistance to:
    - Low or moderate income families; or
    - First-time homebuyers.



# Family Member

- **Family Member** is defined as follows, regardless of actual or perceived sexual orientation, gender identity, or legal marital status:
  - Child, parent, or grandparent;
    - A child is defined as a son, stepson, daughter, or stepdaughter.
    - Parent or grandparent includes a step-parent/grandparent or foster parent/grandparent.
  - Spouse or domestic partner;
  - Legally adopted son or daughter, including a child who is placed with the Borrower by an authorized agency for legal adoption;
  - Foster child;
  - Brother, stepbrother;
  - Sister, stepsister;
  - Uncle;
  - Aunt; **or**
  - Son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, sister-in-law of the Borrower.



## Documenting the Transfer of Gifts

- The Mortgagee must verify and document the transfer of gift funds from the donor to the Borrower.
- Regardless of when gift funds are made available to a Borrower, the Mortgagee must be able to make a reasonable determination that the gift funds were not provided by an unacceptable source, and were the donor's own funds.



# Documenting the Transfer of Gifts

- If the gift funds:
  - Have been verified in the Borrower's account, obtain the donor's bank statement showing the withdrawal and evidence of the deposit into the Borrower's account.
  - Are not verified in the Borrower's account, obtain the certified check or money order or cashier's check or wire transfer or other official check, and a bank statement showing the withdrawal from the donor's account.
  - Are paid directly to the settlement agent, the Mortgagee must verify that the settlement agent received the funds from the donor for the amount of the gift, and that the funds were from an acceptable source.



## Documenting the Transfer of Gifts (cont.)

- If the gift funds:
  - Are being borrowed by the donor and documentation from the bank or other savings account is not available, the Mortgagee must have the donor provide written evidence that the funds were borrowed from an acceptable source, not from a party to the transaction.
  - The Mortgagee and its Affiliates are prohibited from providing the loan of gift funds to the donor unless the terms of the loan are equivalent to those available to the general public.





## Secondary Financing

- Secondary Financing is any financing other than the first mortgage that creates a lien against the property.
- Any such financing that does create a lien against the property is not considered a gift or a grant even if it does not require regular payments or has other features forgiving the debt.



## Secondary Financing (cont.)

	<b>Governmental Entities and HOPE Grantees</b>	<b>HUD-Approved Nonprofits</b>	<b>Family Members</b>	<b>Private Individuals and Other Organizations</b>
<b>Nationwide Mortgage Limits</b>	The insured first mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The insured first mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The insured first mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The Base Loan and secondary financing amounts must not exceed the Nationwide Mortgage Limits for the area in which the property is located.
<b>Secondary Financing for Borrower's MRI</b>	Any secondary financing of the Borrower's MRI must fully comply with the additional requirements in <u>Source Requirements</u> for the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.
<b>CLTV Limitations</b>	No maximum Combined Loan-to-Value (CLTV)	No maximum Combined Loan-to-Value (CLTV)	CLTV ratio of the Base Loan Amount and the secondary financing amount must not exceed 100 percent of the Adjusted Value.	The CLTV ratio of the Base Loan Amount and the secondary financing amount must not exceed the applicable FHA LTV limit.



## Trade-In of Manufactured Housing

- **Trade-In of Manufactured Housing** refers to the Borrower's sale or trade-in of another Manufactured House that is not considered real estate to a Manufactured Housing dealer or an independent third party.
- The net proceeds from the Trade-In of a Manufactured House may be utilized as the Borrower's source of funds.
- Trade-ins cannot result in cash back to the Borrower from the dealer or independent third party.



## Trade-In of Manufactured Housing (cont.)

- The Mortgagee must verify and document:
  - The installment sales contract or other agreement evidencing a transaction; and
  - Value of the trade-in or sale.
- The Mortgagee must obtain independent documentation to support the Trade Equity.



# Sweat Equity

- **Sweat Equity** refers to labor performed, or materials furnished, by or on behalf of the Borrower before closing on the property being purchased.



## Sweat Equity (cont.)

- The Mortgagee may consider the reasonable estimated cost of the work or materials as an acceptable source of funds.
- Sweat Equity provided by anyone other than the Borrower can only be used as an MRI if it meets the **Source Requirements for the Borrower's MRI**.
- The Mortgagee may consider any amount as Sweat Equity that has not already been included in the mortgage amount.
- Cash back to the Borrower is not permitted in Sweat Equity transactions.



## Sweat Equity (cont.)

The Mortgagee **may not** consider the following as **Sweat Equity**:

- Clean up;
- Debris removal;
- General maintenance; and
- Work to be performed using a repair escrow.



# Sweat Equity-Existing Construction-Documentation

- The mortgage must obtain:
  - An appraisal indicating the repairs or improvements to be performed;
  - The source and document the funds for the materials,
  - The Market Value of the materials;
  - Evidence of Contributory Value of the labor either through an appraiser's estimate, or a cost-estimating service; and
  - Documentation and verification that the work will be completed in a satisfactory manner.
- Any work completed or materials provided before the appraisal are not eligible.





# Sweat Equity-Proposed Construction-Documentation

- The mortgage must obtain:
  - An appraisal indicating the repairs or improvements to be performed;
  - The source and document the funds for the materials;
  - The Market Value of the materials,;
  - Evidence of Contributory Value of the labor either through an appraiser's estimate, or a cost-estimating service;
  - The sales contract indicating the tasks to be performed by the Borrower during construction; and
  - Documentation and verification that the work will be completed in a satisfactory manner.
- Any work completed or materials provided before the appraisal are not eligible.



# Manual Underwriting of the Borrower



# Introduction

The **Manual Underwriting of the Borrower** section of the handbook provides Mortgagees FHA's standard general policy requirements to determine a borrower's ability to obtain FHA insured single-family financing considering:

- Credit worthiness;
- Effective income; and
- Assets.

.



# Manual Underwriting Requirements:

The mortgage must manually underwrite those applications where:

- TOTAL issues a Refer;
- Applications that were downgraded to a manual underwrite;  
**or**
- Underwrite those applications for FHA programs for which the program requires manual underwriting.



# General Credit Requirements

- Mortgagees must analyze the following to determine the Borrower's creditworthiness:
  - Credit history;
  - Liabilities; and
  - Debts.



## **Credit Score: Tri-Merged or Residential Credit Report**

- If the Borrower supports a credit score from either a Tri-Merged or a Residential Credit Report, the Borrower must be evaluated based off of traditional credit policies.
- The Mortgagee must utilize the same credit report and credit scores that was used for TOTAL Scorecard evaluation.



# Non-Traditional Credit



## Non-Traditional and Insufficient Credit

- Borrowers without a credit score, the Mortgagee must either obtain a:
  - Non-Traditional Mortgage Credit Report (NTMCR); **or**
  - Independently develop the Borrower's credit history.





# Independent Verification of Non-Tradition Credit Providers

- Mortgagees may independently verify the borrower's non-traditional credit providers.
- The Mortgagee must verify:
  - Through public records the existence of each credit provider;
  - A published address or telephone number for the credit provider; and
  - Obtain the most recent 12 months cancelled checks or equivalent proof of payment.



## Sufficiency of Credit References

- To be sufficient to establish the Borrower's credit, the credit history must include **three credit references**, including at **least one** or more from the list below:
  - Rental housing payments;
  - Telephone service (cellphone is acceptable); and
  - Utilities (not included in rent)
    - Gas;
    - Electric;
    - Water;
    - Television service; and
    - Internet.



# Sufficiency of Credit References

**Two credit references** can be used from list provided below:

- Insurance premiums not payroll deducted
- Payment to child care providers (business)
- School tuition
- Retail store credit cards
- Rent-to-own
- Patient obligation for medical bills
- Savings history for 12 month evidence by regular deposits not payroll deducted resulting in an increased balance to the account that were made at least quarterly without insufficient funds (NSF) reflecting for checking
- Automobile lease
- Personal loan from an individual with repayment terms in writing and payments made supported by cancelled checks



# Sufficiency of Credit References: Authorized User Accounts

- The Mortgagee may use Borrower Authorized User Accounts as a credit reference. The Mortgagee must obtain documentation to evidence that the Borrower:
  - Has been making regular on-time payments during the previous 12 months;
  - Does not have a history of delinquent payments on the loan; and
  - The debt payment is be included in a Borrower's DTI ratio.



# Evaluating Credit History



# Hierarchy of Payment History Evaluation

- The underwriter must evaluate the Borrower's payment histories in the following order:
  - 1) Previous housing expenses and related expenses, including utilities;
  - 2) Installment debts; and
  - 3) Revolving accounts.



## Satisfactory Credit

- The underwriter may consider a Borrower to have an acceptable payment history:

	12 Months	24 Months
Housing and Installment	0 x 30	2 x 30
Revolving	2 x 60, 0 x 90	---



## Case Study: Credit History

	12 Months	24 Months
Mortgage	0 x 30	0 x 30
Charge card	2 x 30	1 x 60
Home Equity	0 x 30	1 x 30
Car Loan	1 x 30	1 x 30
Charge Card	1 x 60	0 x 30
Charge Card	0 x 30	1 x 30





## Case Study: Credit History

	12 Months	24 Months
Mortgage	0 x 30	0 x 30
Charge card	2 x 30	1 x 60
Home Equity	0 x 30	1 x 30
Car Loan	1 x 30	1 x 30
Charge Card	1 x 60	0 x 30
Charge Card	0 x 30	1 x 30



## Satisfactory Credit

The underwriter may consider a Borrower to have an acceptable payment history:

	12 Months	24 Months
Housing and Installment	0 x 30	2 x 30
Revolving	2 x 60, 0 x 90	---



## Payment History Requiring Additional Analysis

- The Mortgagee must analyze the Borrower's delinquent accounts to determine whether **late payments were based on a disregard for financial obligations**, an inability to manage debt, or **extenuating circumstances**.



## Extenuating Circumstances: Clarification

- A list of acceptable Extenuating Circumstances is **not provided** in the Single Family Housing Policy Handbook.
- The underwriter must make the determination if the cause of the credit history was due to a **life changing event that was beyond the Borrower's control and most likely will not reoccur.**
- An example of a life changing event is, death or serious illness of a wage earner who contributes to the support of the household.
- **Divorce is not** to be considered as an **extenuating circumstance.**



## Evaluating: Mortgage History for Modification

- A mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.
- Mortgages in which modifications incorporated deficiency balances, are not considered delinquent.



# Case Study: Mortgage History for Modification

- Mr. Smith has applied for a **Cash-Out Refinance** transaction. He purchased his home in 1999.
- Five months ago, Mr. Smith modified his mortgage and has paid as agreed per his modification agreement. His modification agreement included a deficiency balance.
- Due to a divorce, Mr. Smith fell behind on making his mortgage payments. Up until Mr. Smith's modification agreement, Mr. Smith was 90 days delinquent on his mortgage.
- What is the mortgage payment history for a Cash-Out Refinance?
- What mortgage payment history are we to consider for Mr. Smith?



# Case Study: Mortgage History for Modification (cont.)

- **What is the mortgage payment history we are to consider for a Cash-Out Refinance?**
  - 8. Programs and Products - Refinances
    - v. Cash-Out Refinances
      - (A) Borrower Eligibility
        - (2) Payment History Requirements
          - (a) Standard
- **The Mortgagee must document that the Borrower has made all payments for all their mortgages within the month due for the previous 12 months or since the Borrower obtained the mortgages, whichever is less.**
- Additionally, the payments for all mortgages secured by the subject property must have been paid within the month due for the month prior to mortgage Disbursement.
- Properties with mortgages must have a minimum of six months of Mortgage Payments. Properties owned free and clear may be refinanced as cash-out transactions.



## Case Study: Mortgage History for Modification (cont.)

- What is Mr. Smith's mortgage payment history?
- Program type for which Mr. Smith has applied requires a review for the **previous 12 months** or since the Borrower obtained the mortgages, whichever is less.
- Mr. Smith:
  - 5 months 0 x 30 Since the modification
  - 7 months 7 x 90 Up until Mr. Smith's modification agreement, Mr. Smith was 90 days delinquent





## Case Study: Mortgage History for Modification (cont.)

- Is Mr. Smith's mortgage payment history acceptable for a Cash-Out Refinance?
- **No.**



## Collection Accounts: Medical Collections

- **Medical Collections** are not required to be paid and satisfied.
- The Mortgagee must document reasons for approving a mortgage when the Borrower has any open collection accounts. This includes medical collections.
- The **Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account.** This includes **medical collections.**



# Judgments: Exception Policy Clarification

- The Mortgagee must verify that court-ordered Judgments are resolved or paid off prior to or at closing.
- **Exception:**
  - A Judgment is considered resolved if the Borrower has:
    - Entered into a valid agreement with the creditor to make regular payments on the debt;
    - Has made timely payments for at least three months of scheduled payments; and
    - The Judgment will not supersede the FHA-insured mortgage lien.
- The Borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments.

*Note: All judgment liens must be subordinated.*



## Chapter 7 Bankruptcy: Discharge Period less than 2 Years

- A Chapter 7 bankruptcy (liquidation) does not disqualify a Borrower from obtaining an FHA-insured mortgage if, **at the time of case number assignment** if an elapsed period of **less than two years, but not less than 12 months**, may be acceptable, have elapsed since the date of the bankruptcy discharge if the Borrower:
  - Can show that the bankruptcy was caused by extenuating circumstances beyond the Borrower's control; and
  - Has since exhibited a documented ability to manage their financial affairs in a responsible manner.



## Chapter 13 Bankruptcy: Pay-out Period

- A Chapter 13 bankruptcy does not disqualify a Borrower from obtaining an FHA-insured mortgage if, **at the time of case number assignment, at least 12 months** of the pay-out period under the bankruptcy has elapsed.
- The Mortgagee must determine that during this time, the Borrower's payment performance has been satisfactory and all required payments have been made on time; and the Borrower has received written permission from bankruptcy court to enter into the mortgage transaction.



## Foreclosure and Deed-in-Lieu Period

- A Borrower is generally not eligible for a new FHA-insured mortgage if the Borrower had a foreclosure or a Deed-in-Lieu of foreclosure in the three-year period prior to the **date of case number assignment**.
- The three-year period begins on the date of the Deed-in-Lieu or the date that the Borrower transferred ownership of the property to the foreclosing Entity/designee.



## Foreclosure and Deed-in-Lieu of Foreclosure: Exceptions

- The Mortgagee may grant an exception to the three-year requirement if the foreclosure was the result of documented extenuating circumstances that were beyond the control of the Borrower, such as a serious illness or death of a wage earner, and the Borrower has re-established good credit since the foreclosure.
- Divorce **is not considered** an extenuating circumstance.
- The inability to sell the property due to a job transfer or relocation to another area **does not qualify** as an extenuating circumstance.



## Foreclosure and Deed-in-Lieu: Documentation

- If the credit report does not indicate the date of the foreclosure or DIL of foreclosure, the Mortgagee must obtain the Settlement Statement, deed, or other legal documents evidencing the date of property transfer.
- If the foreclosure or DIL of foreclosure was the result of a circumstance beyond the Borrower's control, the Mortgagee must obtain an explanation of the circumstance and document that the circumstance **was beyond the Borrower's control**.





## Short Sale: Period

- A Borrower is generally not eligible for a new FHA-insured mortgage if they relinquished a property through a short sale within three years from the date of case number assignment.
- The three-year period begins on the date of transfer of title by short sale.



## Exception for Borrower Current at the Time of Short Sale

- A Borrower is considered eligible for a new FHA-insured mortgage if, from the date of case number assignment for the new mortgage:
  - All Mortgage Payments on the prior mortgage were made within the month due for the 12-month period preceding the short sale; and
  - Installment debt payments for the same time period were also made within the month due.



## Exception for Extenuating Circumstances: Short Sale

- The Mortgagee may grant an exception to the three-year requirement if the short sale was the result of documented extenuating circumstances that were beyond the control of the Borrower, such as a serious illness or death of a wage earner, and the Borrower has re-established good credit since the short sale.
- Divorce is not considered an extenuating circumstance.
- The inability to sell the property due to a job transfer or relocation to another area does not qualify as an extenuating circumstance.



## Required Documentation: Short Sale

- If the credit report does not indicate the date of the short sale, the Mortgagee must obtain the Settlement Statement, deed, or other legal documents evidencing the date of property transfer.
- If the short sale was the result of a circumstance beyond the Borrower's control, the Mortgagee must obtain an explanation of the circumstance and document that the circumstance was beyond the Borrower's control.



## Credit Counseling/Payment Plan

- Participating in a consumer credit counseling program **does not disqualify a Borrower** from obtaining an FHA-insured mortgage, provided the Mortgagee documents that:
  - One year of the pay-out period has elapsed under the plan;
  - The Borrower's payment performance has been satisfactory and all required payments have been made on time; and
  - The Borrower has received written permission from the counseling agency to enter into the mortgage transaction.



# Evaluating Liabilities and Debts



## Closed-end Debts Paid Off Within 10 Months

- Closed-end debts do not have to be included if:
  - They will be paid off within 10 months; **and**
  - The cumulative payments of all such debts are less than or equal to 5 percent of the Borrower's gross monthly income.
- The Borrower may not pay down the balance in order to meet the 10-month requirement.



## Case Study

- Patty Page has applied to purchase a home using FHA financing. Patty's following Installment debts are schedule to be paid off within the next 10 months. Patty's gross monthly income is \$6,000.
- Can we excluded these installment payments from her qualifying ratios?**

Student Loan	\$75.00	\$225.00
Student Loan	\$50.00	\$500.00
Car Loan	\$225.00	\$2025.00





## Case Study

- Can we excluded these installment payments from her qualifying ratios?
- Patty's gross monthly income is  $\$6,000 \times 5\% = \$ 300.00$

Student Loan	\$75.00	\$225.00
Student Loan	\$50.00	\$500.00
Car Loan	\$225.00	\$2025.00

- The installment cumulative payments =  $\$ 350.00$
- Can we excluded these installment payments from her qualifying ratios? **NO.**



## Authorized User Accounts

- Accounts for which the Borrower is an authorized user must be included in a Borrower's DTI ratio **unless** the Mortgagee can obtain documentation to evidence:
  - That the primary account holder has made all required payments on the account for the previous 12 months.
  - If less than three payments have been required on the account in the previous 12 months, the payment amount must be included in the Borrower's DTI.



## Timeshares: Clarification

- A Timeshare must be considered an Installment Loan even under the following circumstances, with the Mortgagee providing acceptable documentation to evidence the collateral as a Timeshare:
  - Timeshare is recorded in legal records as real estate;
  - Borrower's credit report identifies the Timeshare as a mortgage account; and
  - Borrower's credit report identifies the Timeshare as a foreclosure.



## Undisclosed Debt

- When a debt or obligation is revealed during the application process that was not listed on the mortgage application and/or credit report, the Mortgagee must:
  - Verify the actual monthly payment amount;
  - Include the payment amount in the agreement in the Borrower's monthly liabilities and debt; and
  - Determine that any unsecured funds borrowed were not/will not be used for the Borrower's MRI.



## Credit Report Inquiries: Written Explanation

- The Mortgagee must obtain a **written explanation** from the Borrower for all inquiries shown on the credit report that were made in the **last 90 Days**.



## Federal Debt (Manual)

- Federal Debt refers to debt owed to the federal government for which regular payments are being made.
- The Mortgagee must include the debt. The amount of the required payment must be included in the calculation of the Borrower's total debt-to-income (DTI).
- The Mortgagee must include documentation from the federal agency evidencing the repayment agreement and verification of payments made, if applicable.



## 30-Day Accounts

- 30-Day Accounts that are paid monthly on time for the past 12 months are not included in the Borrower's DTI.
- If the credit report reflects any late payments in the last 12 months, the Mortgagee must utilize 5 percent of the outstanding balance as the Borrower's monthly debt to be included in the DTI.



## Disputed Derogatory Credit Accounts

- Disputed Derogatory Credit Accounts refer to disputed charge-off accounts, disputed collection accounts, and disputed accounts with late payments in the last 24 months.
- If the Borrower has \$1,000 or more collectively in Disputed Derogatory Credit Accounts, the Mortgagee must include a monthly payment in the Borrower's debt calculation.
- The Mortgagee must derive the same monthly payment amount as stated per policy, as if the credit account was not disputed.





## Collection Accounts

- A **Collection Account** refers to a Borrower's loan or debt that has been submitted to a collection agency by a creditor.
- **Medical Collections** as previously discussed, are not required to be paid, satisfied, or considered in the Borrower's qualifying ratios.
- The Mortgagee must document reasons for approving a mortgage when the Borrower has any open collection accounts. This includes medical collections.



# Income Requirements



# Employment Documentation

## Traditional:

- The Mortgagee must obtain:
  - Copies of the **pay stubs** covering the most recent 30 consecutive day period (if paid weekly or bi-weekly, pay stubs must cover a minimum of 28 consecutive Days) that show the Borrower's year-to-date earnings, and one of the following to verify current employment;
  - A written Verification of Employment (VOE) covering two years; or
  - An electronic verification acceptable to FHA.
- Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.



# Employment Documentation (cont.)

## Alternative:

- The Mortgagee must obtain:
  - Copies of the **pay stubs** covering the most recent 30 consecutive day period (if paid weekly or bi-weekly, **pay stubs** must cover a minimum of 28 consecutive Days) that show the Borrower's year-to-date earnings;
  - Obtain copies of the original IRS W-2 forms from the previous two years; and
  - Document current employment by telephone, sign, and date the verification documentation, and note the name, title, and telephone number of the person with whom employment was verified
- Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.



# Self-Employment Income-Stability

- Income obtained from businesses with annual earnings that are stable or increasing is acceptable.
- If the income from businesses shows a greater than 20 percent decline in Effective Income over the analysis period, the Mortgagee must document that the business income is now stable.
- A Mortgagee may consider **income as stable** after a 20 percent reduction if the Mortgagee can:
  - Document the reduction in income was the result of an extenuating circumstance;
  - The Borrower can demonstrate the income has been stable or increasing for a minimum of 12 months; and
  - The Borrower qualifies utilizing the reduced income.



# Final Underwriting Decision



## HUD Employee Mortgages

- If the mortgage involves a HUD employee, the Mortgagee must condition the loan on the approval of the mortgage by HUD.
- The Mortgagee must submit the case binder to the Processing and Underwriting Division Director at the Jurisdictional HOC for final underwriting approval.



# Uniform Residential Loan Application (URLA) and HUD/VA Addendum to the URLA

- The Mortgagee must obtain the borrower's initial completed signed URLA (Fannie Mae Form 1003/Freddie Mac Form 65) and Page 2 of form HUD-92900-A before underwriting the mortgage application.





## Conditional Approval

- The underwriter must condition the approval of the Borrower on the completion of the final URLA (Fannie Mae Form 1003/Freddie Mac Form 65) and form HUD-92900-A at or before closing if the underwriter relied on an initial URLA and form HUD-92900-A in underwriting the Mortgage.



## Final Underwriting Decision (Total)

The Mortgagee may approve the mortgage as eligible for FHA insurance endorsement if:

- TOTAL Mortgage Scorecard rated the mortgage application as Accept;
- The Mortgagee reviewed the TOTAL Mortgage Scorecard findings, and verified that all information entered into TOTAL Mortgage Scorecard is consistent with mortgage documentation, and is true, complete, and accurate;
- The mortgage meets all FHA requirements applicable to mortgages receiving a rating of Accept from TOTAL Mortgage Scorecard;
- A DE underwriter underwrote the appraisal according to standard FHA requirements; and
- Approved the property as acceptable for FHA single family insurability.



# Final Underwriting Decision (Manual)

- The Direct Endorsement (DE) underwriter is **ultimately responsible for making an underwriting decision** on behalf of their DE Mortgagee in compliance with HUD requirements.



# Documentation of Final Underwriting Review Decision

- The Mortgagee must complete the following documents to evidence their final underwriting decision:
  - Form HUD-92900-LT, FHA Loan Underwriting and Transmittal Summary;
  - Form HUD-92900-A, HUD/VA Addendum to Uniform Residential Loan Application; and
  - Form HUD-92800.5B, Conditional Commitment Direct Endorsement Statement of Appraised Value.



# Form HUD-92900-LT, FHA Loan Underwriting and Transmittal Summary (TOTAL)

- On form HUD-92900-LT, the Mortgagee must:
  - Indicate the CHUMS ID of the underwriter who reviewed the appraisal;
  - Complete the Risk Assessment; and
  - Enter the identification of “ZFHA” in the CHUMS ID.
- When the Feedback Certificate indicates “Accept/Ineligible,” the Mortgagee must document the circumstances or other reasons that were evaluated in making the decision to approve the mortgage in the Remarks section.



# Form HUD-92900-LT, FHA Loan Underwriting and Transmittal Summary (Manual)

- The underwriter must record the following items on form HUD-92900-LT:
  - Their decision;
  - Any compensating factors;
  - Any modification of the mortgage amount and approval conditions under the “Underwriter Comments”; and
  - Their DE Identification Number and signature.



# Ratio Requirements/Acceptable Compensating Factors (Manual)

Lowest Minimum Decision Credit Score	Maximum Qualifying Ratios (%)	Acceptable Compensating Factors
500-579 or No Credit Score	31/43	Not applicable. Borrowers with Minimum Decision Credit Scores below 580, or with no credit score may not exceed 31/43 ratios.  Energy Efficient Homes may have stretch ratios of 33/45.
580 and above	31/43	No compensating factors required.  Energy Efficient Homes may have stretch ratios of 33/45.
580 and above	37/47	<b>One</b> of the following: <ul style="list-style-type: none"> <li>• verified and documented cash Reserves;</li> <li>• minimal increase in housing payment; or</li> <li>• residual income.</li> </ul>
580 and above	40/40	No discretionary debt.
580 and above	40/50	<b>Two</b> of the following: <ul style="list-style-type: none"> <li>• verified and documented cash Reserves;</li> <li>• minimal increase in housing payment;</li> <li>• significant additional income not reflected in Effective Income; and/or</li> <li>• residual income.</li> </ul>



# Form HUD-92900-A, HUD/VA Addendum to Uniform Residential Loan Application

- The Mortgagee must complete form HUD-92900-A as directed in the form instructions.
- The underwriter, an authorized officer of the Mortgagee and Borrower must execute form HUD-92900-A, as indicated in the instructions.





# **Form HUD-92800.5B, Conditional Commitment Direct Endorsement Statement of Appraised Value**

- The underwriter must complete form HUD-92800.5B as directed in the form instructions.



# Notification of Borrower of Approval and Term of the Approval

- The Mortgagee must timely notify the Borrower of their approval. The underwriter's approval or the Firm Commitment is valid for the greater of 90 Days or the remaining life of the:
  - Conditional Commitment issued by HUD; or
  - the underwriter's approval date of the Property, indicated as Action Date on form HUD-92800.5B.



# Documented Scoring Results: Feedback Certification

- The Mortgagee must include in the case binder the last scoring event feedback certification (feedback document) upon which the Mortgagee made its credit decision regardless of credit risk evaluation.



## Summary

- We have reviewed **Underwriting the Borrower Using the TOTAL Mortgage Scorecard**.
- Mortgagees using TOTAL remain solely responsible for prudent underwriting practices and the final underwriting decision.
- The Mortgagee must ensure full compliance with all FHA eligibility requirements.



## Summary (cont.)

- Underwriting requires careful analysis of the many aspects of the mortgage application. Each mortgage is a separate and unique transaction.
- A mortgage transaction that meets minimal standards does not necessarily constitute prudent underwriting. The underwriter should judge the overall merits of the loan application to render a justifiable and documentable decision.



# Single Family Housing Policy Handbook 4000.1 Training Webcast Series



*Thank you for attending.*